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WILLIAM A. MUNDELL
JEFF HATCH-MILLER
MIKE GLEASON
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BRIAN C. McNEIL
EXECUTIVE SECRETARY

ARIZONA CORPORATION COMMISSION

MEMORANDUM

TO: Marc Spitzer, Chairman
William A. Mundell
Jeff Hatch-Miller
Mike Gleason
Kristin K. Mayes

Arizona Corporation Commission

DOCKETED

AUG 06 2004

FROM: Matthew J. Neubert
Director of Securities

DOCKETED BY

CM

DATE: August 2, 2004

RE: In the matter of Robert C. Frost/Robin Frost (S-03493A-03-0000)

CC: Brian C. McNeil, Executive Secretary

AZ CORP COMMISSION
DOCUMENT CONTROL

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RECEIVED

The attached Order of Restitution and Consent to Same in the above-captioned matter resolves allegations that Respondent Robert Frost ("Frost") made unsuitable recommendations by failing to fully appreciate and understand his clients' investment objectives.¹ The Division recommends this proposed settlement because it will achieve several positive results. First, it returns to the investors' losses incurred in their Morgan Stanley Dean Witter ("MSDW") account. These losses essentially represent their investment of certificate of deposit proceeds to MSDW mutual funds. Second, an order is being entered against Frost which will require him to pay \$2,000 to the state of Arizona. Third, it avoids the cost and uncertainties of litigation for both parties.

The Division's allegations in this case involves Frost's recommendation that the investors change their investment portfolio from one almost entirely composed of incoming producing investments; nearly 50% of which were in the form of certificates of deposits, to one where 87% of their assets were invested in seven MSDW proprietary funds including several technology sector funds. At least five of the seven MSDW funds had a primary investment objective of long term growth. Further complicating this matter was the fact that the recommendations were made between December 1999 and March 2000, with the certificate of deposit proceeds being invested during March 2000, just prior to and at the beginning of the market downturn.

¹ Robin Frost was named pursuant to A.R.S. § 44-2031(C) for the purpose of determining the liability of the marital community. This settlement dismisses Robin Frost from the action.

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The central dispute centered on whether the investors fully understood and agreed with Frost's long term growth investment strategy and whether investing 87% of their assets in growth mutual funds, given the investors' history of investing in conservative, low-risk income producing investments was appropriate.

For the reasons set forth in the first paragraph, the Division recommends the Division accept this proposed settlement and issue the proposed Order of Restitution and Consent to Same wherein the investors will receive \$95,000 in restitution and Frost will pay the state \$2,000.

Originator: Phillip Hofling

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DECISION NO.

(ALJ Stern)

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1 4. Before opening their securities accounts at Morgan Stanley in late 1999, the
2 Devenneys derived their monthly retirement income from three primary sources: social security, a
3 small pension fund, and investments maintained in securities accounts at A.G. Edwards.

4 5. The Devenneys held the following securities in their securities accounts at A.G.
5 Edwards as of October 29, 1999: (i) 6,420.295 shares of MFS Series Trust III High Income Fund
6 Class A ("MFS") with a value of \$4.93 per share, and a total value of \$31,652.05; (ii) 3,044.911
7 shares of Mainstay Funds High Yield Corporate Bond Fund Class B ("Mainstay"), with a value of
8 \$7.44 per share, and a total value of \$22,654.14; (iii) a Bankers Trust Subordinated Note in the face
9 amount of \$25,000, and a value of \$23,276.50; and (iv) 53 units of a unit investment trust, UTS
10 Corporate Income Fund #50 Intermediate Series, with a unit price of \$962.59 and a total value of
11 \$51,017.27. The Devenneys also had cash totaling \$36.83. In a separate account at A.G. Edwards,
12 Mrs. Devenney held 377.823 shares of Federated Equity Income Fund Class B with a value of
13 \$20.67 per share, and a total value of \$7,809.60. The Devenneys also owned at this time three
14 Certificates of Deposit ("CDs") that were not custodialized at A.G. Edwards with a value of
15 approximately \$108,000.

16 6. In November 1999, after friends suggested they could improve the performance of
17 their investment assets, and at the recommendation of those friends, the Devenneys contacted and
18 met with ROBERT FROST to discuss transferring assets from A.G. Edwards to Morgan Stanley.

19 7. Two accounts were established for the Devenneys at MSDW: (i) the J. Martin
20 Devenney and Carmen Ann Devenney, Trustees for the Devenney Family Trust Account, (the "Joint
21 Account") and (ii) the Carmen Devenney Retirement Account (the Retirement Account"). In late
22 December 1999, the Devenneys transferred all the assets from their securities accounts at A.G.
23 Edwards to MSDW.

24 8. On January 3, 2000, the Devenneys executed two mutual fund switch letters which
25 authorized Morgan Stanley to liquidate their existing positions in the MFS and Mainstay fixed
26 income mutual funds, and to use the proceeds of those sales to purchase in the Joint Account shares

1 in the MSDW American Opportunities Fund ("Opportunities Fund"). The Opportunities Fund was a
2 mutual fund with a long-term growth objective, which normally invested at least 65% of its assets in
3 common stocks and disclosed in its Prospectus that it could invest up to 35% of its assets in foreign
4 non-exchange traded securities and other investments.

5 9. ROBERT FROST noted on the mutual fund switch letters that the above-referenced
6 transaction was solicited because the customers' "objectives have changed to growth."

7 10. ROBERT FROST also recommended and the Devenneys' also purchased in the Joint
8 Account B shares in three additional mutual funds in January 2000, the MSDW Information Fund,
9 the MSDW Mid-Cap Equity Trust Fund, and the MSDW S&P 500 Index Fund, the first two of
10 which had a primary investment objective of growth. The mutual fund purchases in January 2000 in
11 the Joint Account totaled approximately \$103,000. The remaining assets and funds deposited in the
12 Joint Account, totaling approximately \$17,500, were invested in a MSDW money market fund.
13 Also, at ROBERT FROST'S recommendation in January 2000, Mrs. Devenney purchased in her
14 Retirement Account B shares of MSDW Dividend Growth in the total sum of \$7,654.00.

15 11. In March 2000, at ROBERT FROST's recommendation, the Devenneys deposited
16 into the Joint Account an additional sum of approximately \$108,000 that they previously had
17 invested in CDs. At ROBERT FROST'S recommendation, the Devenneys used those funds to pur-
18 chase B shares in the Van Kampen Technology Fund and the MSDW Small-Cap Growth Fund, and
19 to purchase additional shares in each of the four other mutual funds they already owned in the Joint
20 Account except for the MSDW S&P 500 Index Fund. The Devenneys invested \$95,000 in these five
21 mutual funds in the Joint Account in March of 2000. The balance of the proceeds deposited by the
22 Devenneys into their Joint Account in March of 2000, in the approximate sum of \$13,000, was
23 added to their MSDW money market fund. Thus, by the end of March 2000, the Devenneys had
24 transferred to MSDW substantially all of their investable assets, totaling approximately \$237,000.

25 12. At the time of their initial contact with ROBERT FROST the Devenneys' portfolio
26 was almost entirely comprised of income producing investments; nearly 50% of which were in the

1 form of CDs. By March 31, 2000, however, approximately 87% of the Devenneys' assets were
2 invested in seven mutual funds, five of which had a primary investment objective of long term
3 growth.

4 **II.**

5 **CONCLUSIONS OF LAW**

6 1. The Commission has jurisdiction over this matter pursuant to Article XV of the
7 Arizona Constitution and the Securities Act.

8 2. Frost is subject to Rule R14-4-130(A)(4) of the Securities Act.

9 3. The Commission finds the following relief appropriate and in the public interest.

10 **III.**

11 **ORDER**

12 **IT IS HEREBY ORDERED:**

13 1. FROST shall pay the sum of \$2,000 to the State of Arizona within three business days
14 after FROST completes the payment set forth in paragraph 2 below.

15 2. FROST shall pay to the Commission for distribution to investors identified in the
16 Division's Notice the amount of \$95,000 within five (5) business days from the date of entry of this
17 Order.

18 3. Any failure by FROST to comply with any obligation set forth in this Order shall
19 constitute a violation of this Order and the Commission may, at its sole discretion, vacate this order
20 and restore this case to the active docket or take such other action it deems appropriate.

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1 4. This matter is dismissed against ROBIN FROST subject to ROBERT FROST's
2 fulfillment of his obligations herein.

3 IT IS FURTHER ORDERED that this Order shall become effective immediately.

4 BY ORDER OF THE ARIZONA CORPORATION COMMISSION

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7 CHAIRMAN

COMMISSIONER

COMMISSIONER

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9 COMMISSIONER

COMMISSIONER

10 IN WITNESS WHEREOF, I, BRIAN C. McNEIL,
11 Executive Secretary of the Arizona Corporation
12 Commission, have hereunto set my hand and caused the
13 official seal of the Commission to be affixed at the
14 Capitol, in the City of Phoenix, this ____ day of
15 _____, 2004.

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BRIAN C. McNEIL
Executive Secretary

DISSENT

DISSENT

This document is available in alternative formats by contacting Yvonne McFarland, Executive Assistant to the Executive Secretary, voice phone number 602-542-3931, E-mail ymcfarland@cc.state.az.us

(PAH)

CONSENT TO ENTRY OF ORDER

1
2 1. RESPONDENT ROBERT C. FROST ("FROST"), an individual, admits the
3 jurisdiction of the Commission over the subject matter of this proceeding. FROST acknowledges
4 that he has been fully advised of his right to a hearing to present evidence and call witnesses and
5 FROST knowingly and voluntarily waives any and all rights to a hearing before the Commission and
6 all other rights otherwise available under Article 11 of the Securities Act and Title 14 of the Arizona
7 Administrative Code. FROST acknowledges that this Order for Restitution and Consent to Same
8 ("Order") constitutes a valid final order of the Commission.

9 2. FROST knowingly and voluntarily waives any right under Article 12 of the Securities
10 Act to judicial review by any court by way of suit, appeal, or extraordinary relief resulting from the
11 entry of this Order.

12 3. FROST acknowledges and agrees that this Order is entered into freely and voluntarily
13 and that no promise was made or coercion used to induce such entry.

14 4. FROST acknowledges that he has been represented by counsel in this matter, he has
15 reviewed this Order with his attorney and understands all terms it contains.

16 5. FROST consents to the entry of this Order in the form attached hereto and
17 incorporated by reference herein.

18 6. FROST understands that default shall render him liable to the Commission for its
19 costs of collection and interest at the maximum legal rate.


20 7. FROST agrees that he will continue to cooperate with the Securities Division
21 including, but not limited to, cooperating with the state of Arizona in any related investigation or any
22 other matters arising from the activities described in this Order.

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ROBERT C. FROST

Kathleen P. Carr
NOTARY PUBLIC

 KATHLEEN P. CARR
Notary Public - Arizona
MARICOPA COUNTY
My Commission Expires
January 23, 2006